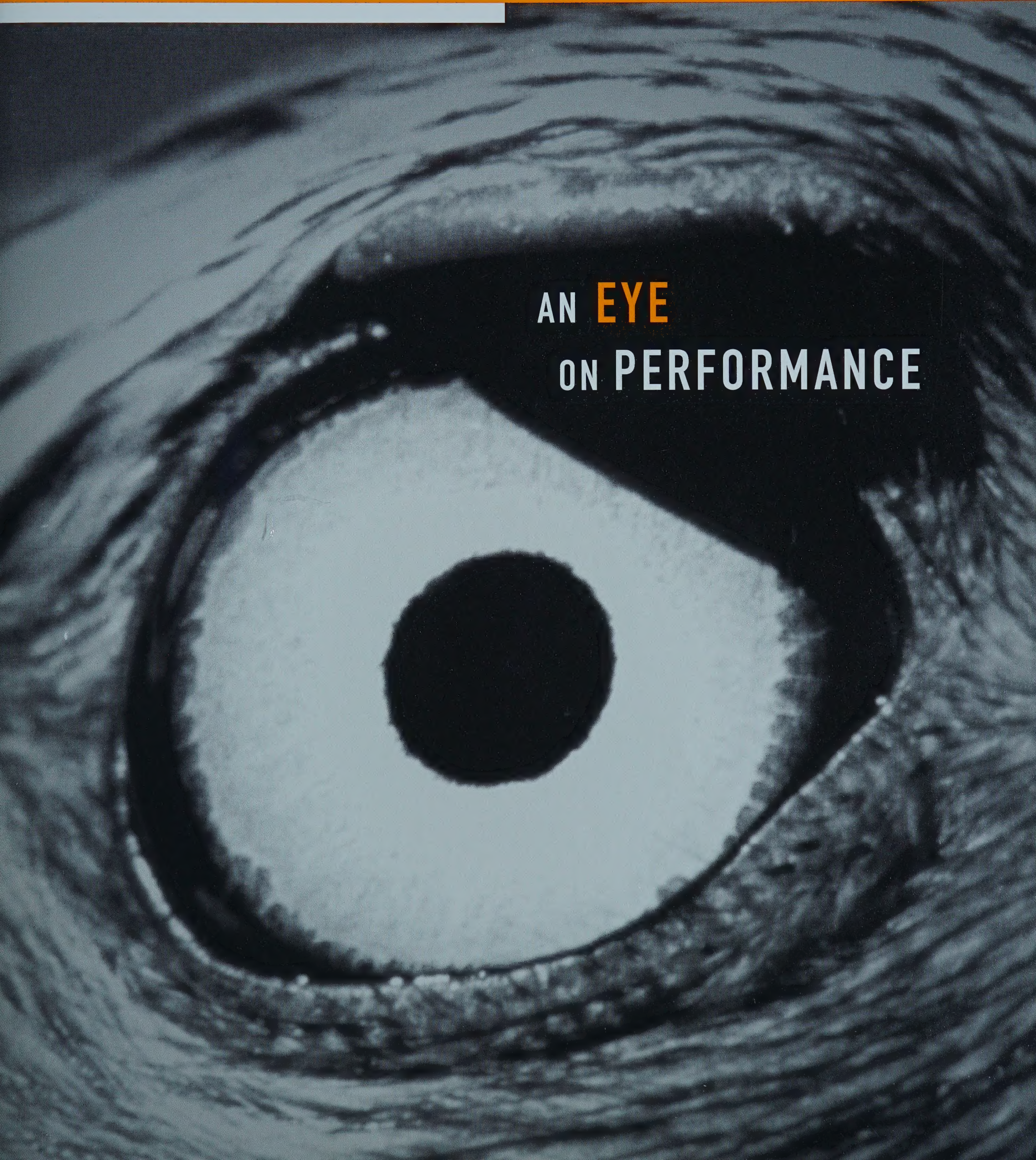
1999 ANNUAL REPORT

# Hawk Oil Inc.



Hawk Oil Inc. is an emerging junior oil and gas exploration and production company operating in Western Canada and headquartered in Calgary, Alberta.



# CORPORATE PROFILE

Hawk was incorporated as a private company in 1996 and completed its initial public offering in 1997. Its shares are listed on the Canadian Venture Exchange (CDNX) under the symbols HWK.A and HWK.B.

In 1999 Hawk experienced its third consecutive year of significant reserves, production and cash flow growth. The Company continues to maintain a large portfolio of low-to-medium risk, internally-generated exploration and development plays. Hawk operates the vast majority of its production and strives to minimize operating, finding and onstream costs. The Company is strategically positioned with a strong balance sheet, excellent cash flow and earnings, large undeveloped land position and a solid management team to take advantage of growth opportunities.

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## ANNUAL MEETING OF SHAREHOLDERS

The Annual General Meeting of Shareholders of Hawk Oil Inc. will be held at 3:30 p.m. on Tuesday, June 6, 2000 at Gowling, Strathy & Henderson, Barristers & Solicitors, 14th Floor, Scotia Centre, 700-2nd Street S.W., Calgary, Alberta.

# HAWK OIL INC. 1999 HIGHLIGHTS

## FINANCIAL

| | 1999 | 1998 | % Change |
|---|---|---|---|
| Gross production revenue | **$ 4,122,180** | $ 1,329,975 | 210 |
| Cash flow | **$ 2,437,051** | $ 507,072 | 381 |
| Earnings | **$ 990,700** | $ 15,638 | 6,235 |
| Capital expenditures | **$ 4,880,787** | $ 5,101,729 | (4) |
| Working capital | **$ (901,405)** | $ 16,750 | (5,382) |
| Bank debt | **$ 1,500,000** | $ nil | – |
| Shares outstanding at year end | | | |
| Class A | **5,375,733** | 5,322,400 | – |
| Class B[1] | **712,752** | 712,752 | – |

[1] Hawk is an "A/B" structured company with Class B Flow-Through shares converting to Class A shares, at the Company's discretion, between July 31, 2000 and July 1, 2002 at a ratio of the $10 Class B share purchase price divided by the Class A share trading price at the time of conversion. As the price of the Class A shares on the CDNX rises, the effective dilution caused by the Class B share conversion diminishes. From this point forward Hawk will report its cash flow, net income and net asset value on a per Class A share basis and on a fully diluted basis. For this reporting period the conversion ratio to be used on the fully diluted basis is based upon the December 31, 1999 Class A share trading price of $1.29 per share. Accordingly, Hawk's fully diluted shares outstanding for this reporting period will be deemed to grow by 5,527,132 shares, a full 28 months before the final conversion date.

## OPERATING

| | 1999 | 1998 | % Change |
|---|---|---|---|
| Average production | | | |
| Crude oil and NGLs (bbls/day) | **202** | 208 | (3) |
| Natural gas (mcf/day) | **2,500** | 54 | 4,530 |
| Oil equivalent (boe/day) | **452** | 213 | 112 |
| Average selling prices | | | |
| Oil ($ per bbl) | **24.75** | 17.01 | 46 |
| Natural gas ($/mcf) | **2.52** | 2.00 | 26 |
| Reserves (Proven) | | | |
| Oil and NGLs (mbbls) | **1,042** | 908 | 15 |
| Natural gas (mmcf) | **11,783** | 6,592 | 79 |
| Barrels of oil equivalent (mboe at 10:1) | **2,220** | 1,567 | 42 |
| Reserve value (15% DCF, $M) | **18,040** | 9,338 | 93 |
| Reserves (proven and probable) | | | |
| Oil and NGLs (mbbls) | **2,077** | 2,000 | 4 |
| Natural gas (mmcf) | **14,765** | 10,575 | 40 |
| Barrels of oil equivalent (mboe at 10:1) | **3,554** | 3,058 | 16 |
| Reserve value (15% DCF, $M) | **23,278** | 13,750 | 69 |
| Undeveloped land (acres) | | | |
| Gross | **24,695** | 14,195 | 74 |
| Net | **19,281** | 9,300 | 107 |
| Wells drilled | | | |
| Gross | **13** | 9 | 44 |
| Net | **12.1** | 7.8 | 55 |
| Success rate | **79%** | 94% | (16) |

**In 1999, Hawk Oil Inc. achieved its third consecutive year of significant growth in reserves, production and cash flow.**



# LETTER TO SHAREHOLDERS

**We continued to deliver reserve and production additions which placed the Company in the industry's top quartile of low-cost producers. Our achievements in 1999 included the following:**

### 1999 COMPANY HIGHLIGHTS

- Drilled 13 (12.1 net) wells, 46 percent of which were exploration, resulting in 10 (9.5 net) producing wells for an overall success rate of 79 percent;
- Replaced 1999 production by 400 percent on a proved reserve basis, primarily through the drill bit;
- Achieved a proved finding and development cost of $5.97 per barrel of oil equivalent (boe);
- Increased earnings by 6,235 percent over 1998 to $990,700;
- Increased average daily production by 112 percent to 452 boe per day;
- Increased cash flow by 380 percent over 1998 to $2,437,051;
- Achieved a proved recycle ratio of 2.56;
- Diversified product mix from 97 percent oil to 56 percent natural gas and 44 percent oil; and
- Created a large, balanced inventory of oil and natural gas prospects, which are ready to be drilled on an undeveloped land inventory of 137,681 net acres.

## GROWTH STRATEGY

Hawk's primary strategy continues to be profitable growth on a per share basis by concentrating on near-term cash flow. The Company targets high-netback products in low-cost areas characterized by year-round access, available existing infrastructure, moderate drilling depths and affordable land costs.

Hawk initiated this strategy in the fall of 1997 by drilling oil wells in West Central and Southeast Saskatchewan, which offered immediate cash flow with high netbacks. However, with the decline of oil prices in early 1998, the Company used its broad skills set to quickly change the direction of its exploration program to natural gas. Since the switch to natural gas in early 1998, the Company has drilled 16 gas prospects, resulting in 14 producing wells.

In late 1999, with the price of crude oil improving, Hawk once again focused on creating a balanced production mix. Capital was directed to oil projects with the acquisition of three-dimensional (3D) seismic programs at Epping and Montmartre and the drilling of three heavy oil wells at Epping and two light oil prospects in Southeast Saskatchewan.

Another aspect of Hawk's strategy is to limit risk exposure. Hawk believes that it is prudent for a junior company to pursue moderate-risk, moderate-reward prospects as opposed to high-risk, high-reward prospects. Accordingly, the Company has concentrated on lower-risk areas such as Vermilion and Epping, resulting in an excellent drilling success rate accompanied by immediate cash flow. As the Company grows, we will increase our exposure to higher-risk, higher-reward prospects. To that end, Hawk has defined numerous high-impact locations that will be drilled once the Company achieves the appropriate size to support higher-risk exposure.

As drilling prospects are developed, Hawk's level of participation in any given play continues to be determined by cost and risk analysis. The Company strives for operatorship and a high working interest in any development or moderate-risk exploration project in order to maintain control over the technical aspects, capital and operating costs. Hawk continues to operate virtually all of its production at an average working interest of approximately 85 percent.

We continue to recognize the importance of a balanced portfolio of opportunities. Part of this balance includes the numerous drillable oil prospects that Hawk has stockpiled. These range from light oil development projects such as horizontal infill and step-out drilling at Glen Ewen, to exploratory drilling at Bromhead and Montmartre, Saskatchewan. The Company also has numerous infill, multi-zone, heavy oil locations at Epping and Northminster. Additionally, Hawk has various drill-ready gas opportunities in Vermilion, Hines and West Edmonton. We are constantly evaluating acquisitions, as well as farm-in opportunities where vertical infill, horizontal infill, step-out or outpost drilling is required to further exploit existing pools or to find new ones.

Hawk continues to keep operating costs and overhead to an absolute minimum. In 1999 Hawk's operating and net overhead costs were $5.64 per boe and $1.67 per boe respectively.

## INDUSTRY OUTLOOK

These are indeed interesting times for the oil and gas industry. Commodity prices for both oil and gas are trading at historic highs. OPEC's reduced production quotas, coupled with rising demand in the Asian and North American markets, have led to anticipated supply shortages and consequently, have significantly strengthened oil prices. On the gas front, rising North American gas consumption driven by fuel switching and electrical demand has resulted in record gas prices.

Despite this rosy outlook for commodity prices, there is a general lack of investor interest in the oil and gas industry. Although this can be attributed to many factors, I believe the primary reason is that many investors are focused on the high technology industries where recent momentum has dramatically increased share prices. These companies are enjoying current share price to earnings (P/E) ratios in the 100-to-500 range while most oil companies are trading in the less-than-20 range. P/E ratios are an important indicator as they provide investors with a sense of how expensive a stock's price is relative to its profits. They also indicate how many years it will take for the Company to earn its stock price. I believe 2000 will see improved investor sentiment towards the oil and gas industry as investors once again seek security in companies and industries that generate current, as opposed to future, profits. The oil and gas sector is at present grossly undervalued and represents a tremendous buying opportunity.

## CORPORATE GOVERNANCE

Hawk is very cognizant of the concerns of both regulators and investors over the integrity of financial and reserve information reported by the oil and gas industry. Accordingly, both Management and the Board of Directors are working together to ensure that our Corporate Governance practices continue to address these issues and provide a reasonable level of comfort that no material misstatement has occurred or will occur. For 1999, Hawk addressed the year-end independent reserve evaluation at the Board level with both Management and the independent engineers, Outtrim Szabo Associates Ltd. The Company already has in place an audit committee, comprised of Board members, to address the accuracy and integrity of our financial reporting with both Management and the independent auditors, PricewaterhouseCoopers LLP. We are committed to providing accurate and reliable information throughout our disclosures.

## 2000 OUTLOOK

Since Hawk's inception in 1997, the Company prudently invested the $8,836,000 raised through two equity offerings, resulting in a current net asset value for the Company of approximately $20,000,000. In 2000, Hawk will continue to grow its net asset value by focusing the bulk of its capital spending and activities on development drilling in Epping, Saskatchewan and Vermilion, Alberta. The Company has a capital budget of $5.0 million for exploration and development drilling, which will be funded primarily from cash flow. During the year, Hawk plans to drill 12 to 14 high working-interest exploration and development wells on internally generated prospects.

Excluding acquisitions, Hawk is forecasting a year-end exit rate of 900 boe per day and cash flow of $4.9 million ($0.92 per Class A share, or $0.45 per fully diluted share) based on a price forecast of US$23.66 per barrel (bbl) West Texas Intermediate (WTI) oil and $2.82 per thousand cubic feet (mcf) for natural gas. We are also currently evaluating larger property and corporate acquisitions that fit our corporate strategy.

Hawk is well positioned to take advantage of the many excellent opportunities available to grow the Company. We have a strong balance sheet with little debt. We maintain a low cost structure with below average finding and development, operating and general and administrative costs. When equity markets improve for oil and natural gas producers, Hawk will consider raising additional capital to fund the drilling of its large inventory of exploration and development opportunities.

## ACKNOWLEDGMENTS

I would like to take this opportunity to offer the Company's sincere thanks to our shareholders, directors, employees and contractors for their continued support during 1999.

*On behalf of the Board of Directors,*

S. Fitzmaurice

**Stephen J. Fitzmaurice**
President and Chief Executive Officer
*Chairman of the Board*
March 22, 2000

**During 1999, Hawk continued to balance its oil and gas production ratio. As a result of low oil prices throughout**

# OPERATIONS REVIEW



**1998 and early 1999, the Company chose to increase its focus on gas prospects. As oil prices strengthened significantly throughout 1999, Hawk began to redirect some capital back to the numerous oil opportunities that had been held in reserve. The Company exited the year producing 56 percent natural gas and 44 percent oil. This was accomplished through the drilling of 13 (12.1 net) wells in Alberta and Saskatchewan.**

In 1999 Hawk drilled six (6.0 net) wells on its Vermilion block and cased five wells as gas producers. The Company drilled one (1.0 net) successful gas well at Hines, Alberta and one (0.6 net) dry hole at West Edmonton. In Saskatchewan, Hawk drilled one (1.0 net) dry hole at Arcola in the third quarter and three (3.0 net) successful oil wells on its Epping property during the fourth quarter. Also in the fourth quarter, Hawk participated in the drilling of one (0.5 net) oil well at Montmartre. The Company operated 92 percent of its drilling activity and enjoyed a success rate of 79 percent. Average yearly production has steadily increased from 64 bbls per day in 1997, to 213 boe per day in 1998, up to 452 boe per day in 1999.

### 1999 GROWTH STRATEGIES

Hawk's success in 1999 was again based on strict adherence to our established growth strategy. The Company's activity during 2000 will be guided by the following key elements:

- **Concentrating** on projects which generate near-term cash flow;
- **Exploring** in areas with low-cost drilling and infrastructure;
- **Exploring** for pools that can be brought onstream quickly;
- **Maintaining** control over capital and operating costs;
- **Concentrating** on areas that are well understood by our technical team;
- **Pursuing** internally generated prospects using sophisticated geophysical technology;
- **Maintaining** high working interests and wherever possible, operatorship;
- **Expanding** our land base within our core areas; and
- **Maintaining** a large balanced inventory of exploration, development and acquisition opportunities.

In late 1999 the Company drilled one (1.0 net) significant natural gas well at Epping, which has added 750 mcf per day to Hawk's production.

Hawk's proved reserves totaled 2.22 million boe as of December 31, 1999. This represents a 42-percent increase in proven reserves over 1998. It also represents a 400-percent replacement of the Company's 1999 production on a proven reserve basis. Hawk's finding and development cost for 1999 is $5.97 per boe for proven reserves. This compares with a cost of $5.58 per boe for proven reserves since the Company's inception and clearly places Hawk in the forefront of consistent low-cost explorers.

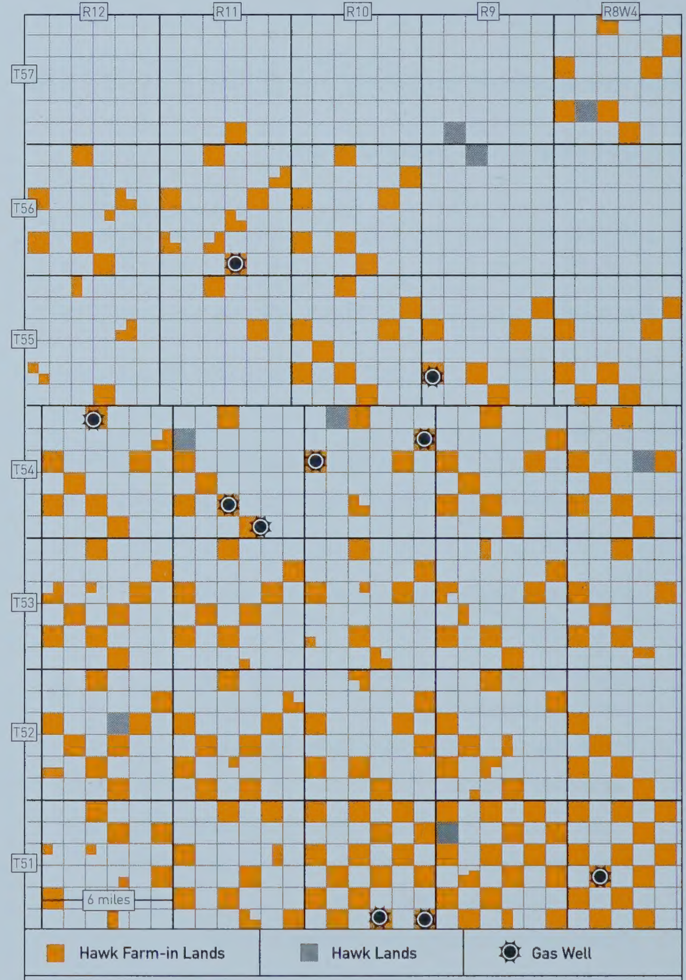
During 1999, Hawk increased its land inventory outside Vermilion to 35,434 gross (26,552 net) acres from 21,750 gross (14,950 net) acres in 1998 with the majority of the acreage or 24,695 (19,281 net) acres undeveloped. Additionally, Hawk holds an interest (100 percent before payout and 50 percent after one-half project payout) in a large farm-in acquired from a major company. The block comprises 118,400 acres of undeveloped land in the Vermilion area of East Central Alberta. Hawk pays **no** royalties on this block, which results in exceptional netbacks to the Company.

## KEY PROPERTIES

**Vermilion:** In July 1998, Hawk acquired an interest in a 125,000 acre block of land in the Vermilion, Alberta area from a major company. Under the first phase of this farm-in, Hawk committed to drill five wells in order to hold all the land until December 31, 1998. Under the second phase, the Company committed to drill four additional wells, which held the block for 1999. For the third phase, Hawk has committed to drill four additional wells, which will hold the block through 2000. The terms of each phase remain the same. When one half of all drilling costs incurred during a particular phase including seismic, drilling, completion, equipping and abandonment costs are recovered, Hawk's 100-percent interest reverts to 50 percent for that phase. After the third phase, the Company has the right to negotiate further drilling phases under the farm-in. The most notable part of this joint venture is that the Company pays neither lessor nor over-riding royalties on these lands and has continual access to 1,100 kilometres of seismic data over the block.

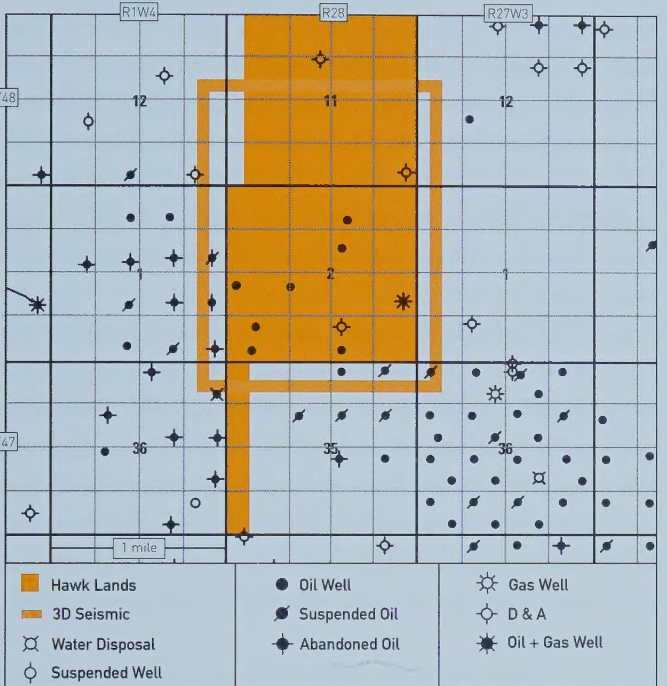
During 1999, Hawk fulfilled its Phase 2 commitment by drilling five (5.0 net) successful natural gas wells. A sixth well (1.0 net) was drilled, however, uneconomic quantities of gas were encountered and the well was subsequently abandoned. Results to date have exceeded Hawk's internal expectations and confirmed the Company's technical models in the area. Hawk encountered natural gas in the Viking, Colony, Waseca, Sparky and Wabiskaw Formations, with production from the wells ranging from 200 mcf per day to 1.5 million cubic feet (mmcf) per day. Hawk is also currently formulating plans to pursue deeper targets in this area.

Hawk is achieving outstanding netbacks from the Vermilion property, currently exceeding $2.50 per mcf as a result of favourable farm-in terms, inexpensive operating costs and high natural gas prices. The Company is currently producing 2.0 mmcf per day (net) from the block; however, productive capability is in excess of 4.0 mmcf per day (net). When Hawk began exploring on the Vermilion block in late 1998, considerable capacity remained in all gas processing facilities. Sharply increased prices in 1999, coupled with Hawk's significant nearby success, resulted in dramatically increased drilling activity within the block. By mid-1999, specific processing facilities began running at maximum levels, which in turn significantly reduced the available capacity for Hawk's gas. The Company has been working diligently with operators in the affected areas to increase capacity and has recently seen production levels climb. Production levels were also impacted by high gas prices in another way; high netbacks resulted in reaching payout on Phase 1 after only five months of production after which the farmor converted to a 50-percent working interest.




**VERMILION AREA**

Numerous drilling opportunities remain on this large block of land. Hawk will focus its future efforts in areas where capacity in gas plants is available. The Company is confident this area will continue to provide superb growth to Hawk.




EPPING AREA

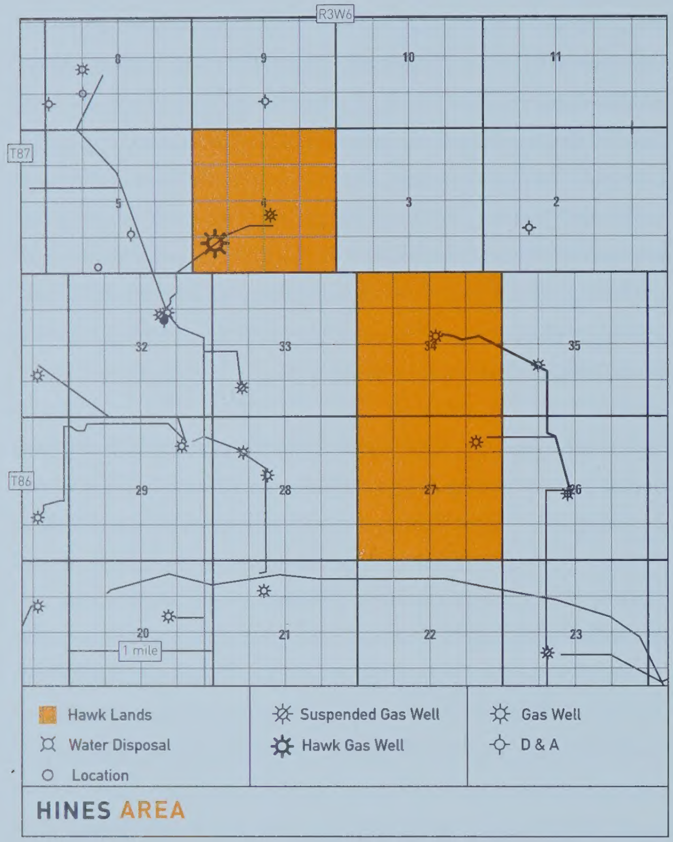
**Epping:** Hawk holds a 100-percent working interest in 1,385 acres, seven heavy oil wells and one natural gas well at Epping, Saskatchewan. This acreage lies south of Lloydminster and was acquired at Crown land sales on an internally generated prospect. Production in this region is associated with stacked sands of the Mannville Group, which all display excellent reservoir characteristics. Three wells were drilled on this property in late 1997. Significant oil reserves were discovered in four different Mannville horizons. Natural gas was also encountered in two additional zones on this acreage. However, commodity prices precluded any further development activity until the second half of 1999.

During 1999, Hawk shot a 3D seismic survey over most of the Epping property to assist in unraveling the complexities associated with numerous stacked pay zones. In the third quarter Hawk re-entered an old abandoned well to test what appeared to be a missed pay zone. The well was perforated and is presently producing 40 bbls per day. Late in the fourth quarter the Company drilled another successful heavy oil well and targeted a 3D-defined natural gas anomaly with a second well. This well encountered a significant gas pay zone, which showed no depletion on an extended high-rate flow test. The well has been placed on production at restricted rates between 750 mcf per day and 1.0 mmcf per day. Two stepout wells were drilled late in the first quarter 2000 at Epping. They displayed multi-zone pay on well logs, including a formation that has demonstrated prolific production on acreage adjacent to Hawk. This new pool is evident on the 3D seismic shot by the Company and will be pursued after spring breakup.

Current production from the Epping property is 225 boe per day of which the majority is 18 degree API oil. Netbacks are presently $16.50 per bbl as a result of low water production, sufficient associated gas to run equipment and high oil prices. To date Hawk has achieved a 100 percent drilling success rate at Epping with a minimum of 12 additional locations on the acreage having been identified using the 3D seismic data. This does not include redrills for multiple zones or downspacing as has been done on adjacent acreage. Nine wells are planned for this property during the current year. We expect that Epping will have a major impact on Hawk's bottom line for the year 2000.

**Hines/West Edmonton:** Over the past 18 months Hawk has expanded its search for gas to include opportunities wherever a significant positive financial impact could be achieved. Hawk is a nimble, technically strong company that has been successful over a wide geographic area.

In late 1998, the Company acquired a section of land adjacent to a prolific, multi-zone, shallow producing field at Hines. Hawk drilled a (1.0 net) successful, multi-zone gas well in January of 1999. This well has been on production since March 1999 and is still producing at a stable rate of 800 mcf per day. Hawk has added another 1,280 acres to its land base adjacent to the Hines field and is continuing to evaluate and develop opportunities in this highly gas-prone area. In the West Edmonton area, Hawk has developed a number of Cretaceous gas prospects and chose to drill two in 1999. At Glenevis, the Company drilled one (1.0 net) multi-zone prospect in March which will be completed




Over the past year, Hawk has been stockpiling a number of other light oil opportunities in Southeast Saskatchewan while the Company focused its efforts on gas exploration. A window of opportunity arose during the third quarter on a Mississippian play in the Arcola area. When a larger block of land became available, the Company drilled one well (1.0 net) which encountered uneconomic quantities of oil and was subsequently abandoned.

Later in the year, Hawk participated in a vertical Red River test (0.5 net) within the Montmartre pool. The well encountered anomalously low-permeability reservoir rock and production quickly dropped from 150 bbls per day to 60 bbls per day with low water cuts. The operator of the play has continued drilling a number of horizontal wells directly offsetting Hawk acreage to the north and south. The Company has chosen to monitor offsetting activity before proceeding with further development.

after spring breakup. A second prospect (0.6 net) was drilled at Atim, immediately west of Edmonton, however, hydrocarbons were not encountered and the well was subsequently abandoned.

## SOUTHEAST SASKATCHEWAN

**Glen Ewen:** At Glen Ewen, which is operated by Hawk, the Company chose to delay shooting seismic and drilling during 1999. Instead, Hawk used the time to consolidate its land position and the Company now holds an average working interest of 91 percent in 880 acres. The property is currently producing 20 bbls per day of light oil from vertical wells through a Company-owned facility. The productive zone is the Frobisher Formation that was deposited as a series of shallow water, high energy shoals trapped updip by impermeable, muddy, evaporitic sediments. During the first quarter 2000, Hawk is shooting a 3D seismic program over the entire property. Immediately following spring breakup the Company is planning to drill a horizontal well in the pool to be followed, if successful, by one or more later in the year.

## EXPLORATION REVIEW

The past year has seen the development of a unique situation in the Western Canadian upstream oil and gas business. Commodity prices at the end of the year had climbed to near record highs while the equity of most junior and intermediate producing companies traded at historic low price to cash flow multiples. This lack of interest in junior equities has translated into poor access to new capital, which in turn has forced most smaller companies to very carefully manage spending.

In Hawk's case, a restrained exploration and development program resulted and the Company has not grown as quickly as it could have with better access to capital. However, this situation has enabled the Company to stockpile numerous prospects and spend its limited capital on the most profitable opportunities.

**Success Rate:** During 1999, Hawk demonstrated a 79-percent drilling success rate with exploration drilling comprising 46 percent of the total. The emphasis on drilling for natural gas marked the first half of the year. In the second half of 1999, as oil prices showed sustainable strength, Hawk focused on creating a balanced production mix. Capital was directed towards 3D seismic at Epping and Montmartre and the drilling of three heavy oil wells in Epping and two light oil prospects in Southeast Saskatchewan.

**Future Activity:** Looking forward to the year 2000, Hawk intends to employ the same growth strategies that have been successful for the Company in the past. At Vermilion Hawk will continue to utilize the extensive farmor seismic database to identify leads. Additional two-dimensional (2D) seismic will be shot to create drill-ready prospects only where plant capacity will allow immediate processing. At present, four (4.0 net) wells are planned for the block during the latter half of the year. Another multi-zone gas prospect was drilled (1.0 net) at Glenevis late in the first quarter. This well encountered six metres of pay in the Banff formation. Drill stem tests were encouraging and an extended flow test will be performed through a nearby gas plant following spring breakup.

At Epping, Hawk intends to drill a minimum of nine wells (8.25 net) on this multi-zone property. Notably, this heavy oil property produced positive cash flow throughout 1998 into early 1999, a period of depressed oil prices. This was as a result of the low operating costs associated with the property. It is Hawk's opinion that numerous high-impact prospects, such as Epping, remain to be exploited in the Lloydminster area. The Company will be selectively pursuing such opportunities. At Glen Ewen in Southeast Saskatchewan, Hawk is shooting a 3D seismic program during the first quarter, to be followed immediately after spring breakup by the first of two (2.0 net) budgeted horizontal wells. Depending on results, a number of follow-up locations may be drilled late in the year.

**New Opportunities:** Hawk is an agile company that is constantly evaluating new prospects, which if technically strong, could alter drilling plans. The Company's size means that many prospects viewed by much of the industry as too small, are able to have a major impact on Hawk's production, cash flow and net earnings.

At the present time, Hawk has a large inventory of internally generated opportunities. This allows the Company to be very selective when planning this year's drilling program. As the Company grows, the search for new plays will include areas that can demonstrate longer-life reserves. Hawk has proven itself to be an efficient, low-cost explorer and producer. Going into the year 2000, the Company is in a strong financial position, allowing for great flexibility to pursue a wide variety of high-impact growth opportunities.

## DRILLING SUMMARY

During 1999, Hawk participated in the drilling of 13 (12.1 net) wells, 46 percent of which were classified as exploration, resulting in 10 (9.5 net) producers for an overall success rate of 79 percent. Hawk was the operator of 12 of the 13 wells (92 percent).

### Drilling Activity by Area

| Property | 1999 Wells Drilled |
|---|---|
| Southeast Saskatchewan | **2** |
| Epping, Saskatchewan | **3** |
| Vermilion, Alberta | **6** |
| West Edmonton, Alberta | **1** |
| Hines, Alberta | **1** |
| Total | **13** |

### Drilling Activity (number of wells)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| Year ended December 31 | **Gross** | **Net** | Gross | Net |
| Oil | **3.0** | **2.5** | 1.0 | 1.0 |
| Natural gas | **7.0** | **7.0** | 7.0 | 6.3 |
| Dry | **3.0** | **2.6** | 1.0 | 0.5 |
| Total | **13.0** | **12.1** | 9.0 | 7.8 |
| Exploratory | **6.0** | **5.6** | 7.0 | 5.8 |
| Development | **7.0** | **6.5** | 2.0 | 2.0 |
| Success rate (%) | | **79** | | 94 |

## LAND HOLDINGS

As a junior company, Hawk recognizes the importance of a large undeveloped land base and has continued to accumulate land in strategic areas. Hawk currently holds approximately 35,434 acres (26,552 net) of land, 24,695 acres (19,281 net) of which are undeveloped. The above mentioned figures do not include the Company's Vermilion block farmin land comprising 118,400 net acres of undeveloped land.

### Land Holdings

| | 1999 | | | 1998 | | |
|---|---|---|---|---|---|---|
| (Acres) | **Gross** | **Net** | **WI%** | Gross | Net | WI% |
| Developed | **10,739** | **7,271** | **68** | 7,555 | 5,650 | 75 |
| Undeveloped | **24,695** | **19,281** | **78** | 14,195 | 9,300 | 66 |
| Vermilion farm-in undeveloped | **118,400** | **118,400** | **100** | 124,800 | 124,800 | 100 |
| Total | **153,834** | **144,952** | **94** | 146,550 | 139,750 | 95 |

### Undeveloped Land Holdings

| | | 1999 | |
|---|---|---|---|
| (Acres) | **Gross** | **Net** | **WI%** |
| Southeast Saskatchewan | **8,064** | **7,492** | **93** |
| Glen Ewen, Saskatchewan | **684** | **489** | **72** |
| Montmartre, Saskatchewan | **2,934** | **2,026** | **69** |
| West Central, Saskatchewan | **1,280** | **1,280** | **100** |
| Epping, Saskatchewan | **1,250** | **1,250** | **100** |
| West Edmonton, Alberta | **2,803** | **1,784** | **64** |
| Hines, Alberta | **1,280** | **1,280** | **100** |
| Vermilion, Alberta | **4,480** | **4,480** | **100** |
| Vermilion Farmin, Alberta | **118,400** | **118,400** | **100** |
| Bear Flat, B.C. | **1,920** | **480** | **25** |
| Total | **143,095** | **137,681** | **96** |

## PRODUCTION SUMMARY

During 1999, the Company continued to build up a production base on its core areas of Vermilion and Epping. In 2000, Hawk expects to add significant production at Vermilion, Epping and Glen Ewen.

### 1999 Average Production Summary

| Property | Working Interest (%) | Net Gas Production (mcfd) | Net Oil Production (bopd) | Net Total Production (boed) |
|---|---|---|---|---|
| Hines | 100 | 613 | – | 61 |
| Vermilion | 75 | 1,696 | – | 170 |
| West Edmonton | 100 | 191 | 3 | 22 |
| Epping | 100 | – | 82 | 82 |
| Queensdale | 100 | – | 100 | 100 |
| Glen Ewen | 50 | – | 9 | 9 |
| Southeast Saskatchewan | 50 | – | 8 | 8 |
| Total | | 2,500 | 202 | 452 |

## RESERVE SUMMARY

Hawk's reserves have been evaluated effective December 31, 1999 by the independent engineering firm of Outtrim Szabo Associates (Outtrim). The following tables summarize the findings of the Outtrim report on an escalated prices basis.

### Reserve Summary

| | Remaining Reserves | | Net Present Value Before Income Tax Discounted | | | |
|---|---|---|---|---|---|---|
| | Crude Oil (mbbls) | Natural Gas (mmcf) | 0% (M$) | 10% (M$) | 15% (M$) | 20% (M$) |
| Total proven | 1,042 | 11,783 | 37,412 | 21,561 | 18,040 | 15,625 |
| Probable | 1,035 | 2,982 | 20,083 | 7,277 | 5,238 | 4,013 |
| Proven + probable | 2,077 | 14,765 | 57,495 | 28,838 | 23,278 | 19,638 |
| Proven + 1/2 probable | 1,559 | 13,274 | 47,454 | 25,200 | 20,659 | 17,632 |

### Price Forecasts used by Outtrim

| | Crude Oil | | Natural Gas |
|---|---|---|---|
| | WTI at Cushing Oklahoma ($US/bbl) | Light Crude at Edmonton ($CDN/bbl) | Alberta Spot ($Cdn/mmbtu) |
| 2000 Q1 | 29.50 | 41.80 | 3.20 |
| 2000 Q2-Q4 | 25.50 | 36.01 | 3.20 |
| 2001 | 21.32 | 29.93 | 2.85 |
| 2002 | 20.60 | 28.44 | 2.70 |
| 2003 | 20.91 | 28.43 | 2.78 |

In 1999, Hawk Oil was very successful at adding new reserves with a net drilling success rate of 79 percent and a proven drilling finding and development cost of $5.97 per boe. Hawk was also successful in converting some of its 1998 probable reserves to 1999 proven reserves through drilling.

### Reserve Reconciliation

| | Crude Oil (mbbls) | | | Natural Gas (mmcf) | | |
|---|---|---|---|---|---|---|
| | Proven | Probable | Total | Proven | Probable | Total |
| December 31, 1998 | 908 | 1,093 | 2,000 | 6,592 | 3,984 | 10,575 |
| Discoveries and extensions | 345 | 88 | 433 | 8,024 | 840 | 8,864 |
| Purchases | 11 | 0 | 0 | 0 | 0 | 0 |
| Production | 72 | 0 | 72 | 921 | 0 | 921 |
| Revisions of prior estimates | (150) | (146) | (284) | (1,912) | (1,842) | (3,753) |
| December 31, 1999 | 1,042 | 1,035 | 2,077 | 11,783 | 2,982 | 14,765 |

### Finding and Development Costs

| | **1999** | 1998 | 1997 | 97-99 |
|---|---|---|---|---|
| Capital expenditures ($ thousands) | **4,881** | 5,102 | 3,800 | 13,783 |
| Proven reserve additions (mboe) | **818** | 589 | 1,056 | 2,470 |
| Proven finding and development costs ($/boe) | **5.97** | 8.67 | 3.60 | 5.58 |
| Proven + probable reserve additions (mboe) | **660** | 748 | 2,388 | 3,804 |
| Proven + probable finding and development costs ($/boe) | **7.40** | 6.82 | 1.59 | 3.62 |
| Established reserve additions (mboe) | **739** | 668 | 1,730 | 3,137 |
| Established finding and development costs ($/boe) | **6.61** | 7.64 | 2.20 | 4.39 |

### RECYCLE RATIO

The recycle ratio provides a measure of a company's ability to sustain growth. It is calculated by taking the Company's cash flow netback on a boe basis and dividing it by the proved finding and development cost ($14.94 per boe / $5.97 per boe). For 1999, Hawk Oil achieved a recycle ratio of 2.50 which is well above industry average.

# MANAGEMENT'S DISCUSSION & ANALYSIS

## FINANCIAL SUMMARY

The operating results for the 1999 calender year were as follows:

**Operating Income** ($)

| Year ended December 31 | **1999** | 1998 |
|---|---|---|
| Petroleum and natural gas revenue | **4,260,341** | 1,290,157 |
| Tariffs | **141,711** | 2,087 |
| Royalties and mineral taxes | **446,553** | 231,779 |
| Production expenses | **929,873** | 429,268 |
| Operating income | **2,742,204** | 627,023 |
| Daily production volume boe | **452** | 213 |
| Sales price | **24.96** | 16.55 |
| Royalties and mineral taxes | **2.71** | 2.98 |
| Production expenses | **5.64** | 5.52 |
| Netback per boe | **16.61** | 8.06 |

In 1999, the Company's operating income showed improvements in most categories. Hawk's sale price was vastly improved over 1998 as a result of improved oil and gas prices. The average selling price of crude oil for 1999 was $24.75, an increase of 46 percent from $17.01 per bbl in the same period in 1998. Natural gas prices also improved significantly in 1999 averaging $2.52 per mcf, an increase of 26 percent from $2.00 per mcf in 1998.

Royalties on a boe basis, net of ARTC, for the year ended December 31, 1999, decreased nine percent to $2.71 per boe from $2.98 per boe in 1998. The reduced royalty can be attributed to a larger portion of Hawk's production originating from the royalty-free Vermilion area. In 1999, Vermilion production accounted for 38 percent of Hawk's total production compared to three percent in 1998.

Production expenses on a boe basis for the year ended December 31, 1999 were essentially unchanged from 1998.

**Capital Expenditures**

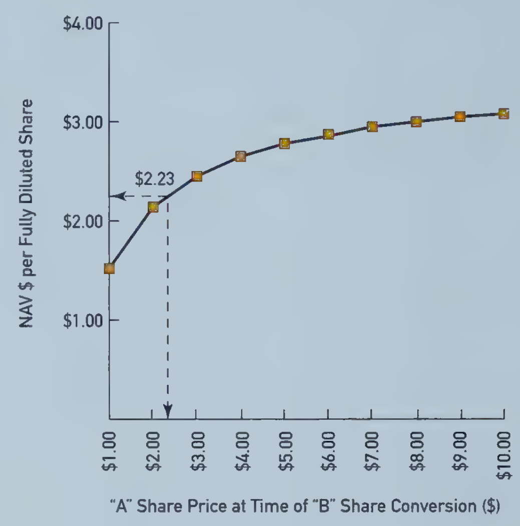
| ($ thousands) | **1999** | 1998 |
|---|---|---|
| Exploration and development | **3,773** | 3,631 |
| Facilities | **748** | 881 |
| Land | **348** | 586 |
| Other | **12** | 4 |
| Total capital expenditures | **4,881** | 5,102 |

Hawk's capital expenditure program for the year ended December 31, 1999 totalled $4,881,000. This amount was funded by cash flow and available bank credit facilities.

## NET ASSET VALUE

As at December 31, 1999, Hawk's net asset value (NAV) was $19,703,670 basic or $19,991,970 fully diluted (including proceeds from the exercise of all outstanding stock options and warrants). This value is based on an independent evaluation of the Company's established reserves, discounted at 15 percent.

The chart herein shows Hawk's current NAV on a fully diluted per share basis assuming various B share conversion prices. In the worst case scenario, whereby Hawk's A shares are trading at less than $1.00 at the time of conversion, Hawk's fully diluted NAV equates to $1.55 per share. In an optimistic case, whereby Hawk's A shares are trading at $10.00 at the time of conversion, Hawk's fully diluted NAV equates to $3.08 per share. If Hawk traded at its actual NAV and the B shares were converted accordingly, then Hawk's fully diluted NAV would equate to $2.23 per share.




| Year ended December 31 | 1999 | 1998 |
|---|---|---|
| Established reserves discounted at 15% before tax | **$ 20,659,000** | $ 12,020,000 |
| Undeveloped acreage ($75/acre) | **1,446,075** | 697,500 |
| Debt plus working capital | **(2,401,405)** | 16,750 |
| Net asset value (basic) | **19,703,670** | 12,734,250 |
| Proceeds from the exercise of outstanding stock options and warrants | **288,300** | 362,080 |
| Net asset value (fully diluted) | **19,991,970** | 13,096,330 |
| Outstanding A shares | **5,375,733** | 5,322,400 |
| Outstanding B shares | **712,752** | 712,752 |
| Outstanding stock options and warrants | **393,000** | 501,280 |
| Net asset value per Class A | **3.66** | 2.39 |
| Net asset value (fully diluted) per share with B shares converted to A shares at Dec. 31 closing price of $1.29 | **$ 1.77** | $ 1.06 |

This net asset value does not include any value associated with the right to drill and explore on 118,400 net acres of undeveloped land in the Vermilion area.

## GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses for the year ended December 31, 1999 increased 22 percent to $275,916 ($1.67 per boe) from $225,372 ($2.90 per boe) for the same period in 1998. This increase reflects increased staff and consulting services which occurred as a result of increased production and activity over 1998. The Company also capitalized $360,353 in overhead related costs to petroleum and natural gas properties and equipment.

## DEPLETION AND AMORTIZATION

Depletion and amortization for the year ended December 31, 1999 increased 91 percent to $727,309 from $380,569 during the same period in 1998. The increase is attributed to a significant increase in annual production volumes. On a boe basis, the depletion and amortization rate decreased 10 percent from 1998. This improvement is a result of the Company adding proven reserves at a low finding and development cost.

The Company's 1999 site restoration costs increased 130 percent over 1998 as a result of new wells being drilled which will require site restoration costs once they have finished producing.

**Depletion and Amortization**

| | **1999** | | 1998 | |
|---|---|---|---|---|
| **$** | **$** | **$/boe** | $ | $/boe |
| Depletion and amortization | **727,309** | **4.41** | 380,569 | 4.89 |
| Site restoration | **20,683** | **0.13** | 9,000 | 0.12 |
| Total | **747,992** | **4.54** | 389,569 | 5.01 |

## WORKING CAPITAL AND CAPITAL REQUIREMENTS

At December 31, 1999, Hawk had a working capital deficiency of $901,405 and bank debt of $1,500,000. In 2000, Hawk will fund the vast majority of its $5.0 million capital program through internally generated cash flow. The Company has no immediate plans to raise additional funds through the equity markets.

## DEBT

On December 31, 1999, the Company's bank debt consisted of a line of credit with the National Bank of Canada for $3,100,000 at an interest rate of prime plus one half percent. As of December 31, 1999 $1,500,000 was outstanding. The Company is in the process of establishing an operating and acquisition credit facility of $11,000,000 with the National Bank of Canada.

## YEAR 2000

The impact of the Year 2000 issue may be experienced before, on, or after January 1, 2000. Hawk currently uses no internal computer systems or applications which could misinterpret this critical change of date. Our accounting and land systems are manual, but if we should convert to an automated system, we will ensure this issue is resolved before they are installed. Hawk has already ensured that computer systems and applications being used by our suppliers are Year 2000 compliant.

# AUDITORS' REPORT

**To The Shareholders of Hawk Oil Inc.**

We have audited the balance sheet of **Hawk Oil Inc.** as at December 31, 1999 and 1998 and the statements of operations and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1999 and 1998 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Calgary, Alberta,
March 16, 2000

Chartered Accountants

# BALANCE SHEET

| As at December 31 | | 1999 | | 1998 |
|---|---|---|---|---|
| **Assets** | | | | |
| Current | | | | |
| Cash and short term deposits | $ | - | $ | 1,428,423 |
| Accounts receivable | | 598,218 | | 347,086 |
| Prepaid expenses | | 44,062 | | 14,194 |
| | | 642,280 | | 1,789,703 |
| Capital assets (Note 2) | | 9,006,427 | | 5,935,144 |
| | $ | 9,648,707 | $ | 7,724,847 |
| **Liabilities and Shareholders' Equity** | | | | |
| Current | | | | |
| Bank indebtedness | $ | 72,880 | $ | - |
| Accounts payable and accrued liabilities | | 1,470,805 | | 1,772,953 |
| | | 1,543,685 | | 1,772,953 |
| Bank debt (Note 3) | | 1,500,000 | | - |
| Provision for site restoration | | 30,412 | | 9,729 |
| Deferred income taxes | | 492,886 | | - |
| | | 3,566,983 | | 1,782,682 |
| Shareholders' equity | | | | |
| Share capital (Note 4) | | 5,066,577 | | 5,917,718 |
| Retained earnings | | 1,015,147 | | 24,447 |
| | | 6,081,724 | | 5,942,165 |
| Contingency (Note 6) | | | | |
| Commitment (Note 7) | | | | |
| | $ | 9,648,707 | $ | 7,724,847 |

*Approved on behalf of the Board:*

M. Yaaikh — Director

S. Fitzmaurice — Director

See accompanying notes

# STATEMENT OF OPERATIONS AND RETAINED EARNINGS

| For the Year Ended December 31 | 1999 | 1998 |
| --- | --- | --- |
| **Revenue** | | |
| Petroleum and natural gas sales, net of royalties | **$ 3,813,788** | $ 1,099,278 |
| Other income | **13,087** | 105,122 |
| | **3,826,875** | 1,204,400 |
| **Expenses** | | |
| Operating | **1,071,583** | 471,956 |
| General and administrative | **275,916** | 225,372 |
| Interest | **42,325** | - |
| Depletion and amortization | **747,992** | 389,569 |
| | **2,137,816** | 1,086,897 |
| Earnings before provision for income taxes | **1,689,059** | 117,503 |
| Deferred income taxes (Note 5) | **(698,359)** | (101,865) |
| Earnings | **990,700** | 15,638 |
| Retained earnings, beginning of year | **24,447** | 8,809 |
| Retained earnings, end of year | **$ 1,015,147** | $ 24,447 |
| Basic earnings per Class A shares | **$ 0.19** | $ 0.00 |
| Basic earnings per Class A and Class B shares | **$ 0.09** | $ 0.00 |
| Fully diluted earnings per Class A and Class B shares | **$ 0.09** | $ 0.00 |

See accompanying notes

# STATEMENT OF CASH FLOWS

| For the Year Ended December 31 | 1999 | 1998 |
|---|---|---|
| **Operating Activities** | | |
| Earnings | $ 990,700 | $ 15,638 |
| Add items not affecting cash | | |
| Depletion and amortization | 747,992 | 389,569 |
| Deferred income taxes | 698,359 | 101,865 |
| | 2,437,051 | 507,072 |
| Net change in non-cash working capital in operating activities | | |
| Accounts receivable | (251,132) | 117,343 |
| Prepaid expenses | (29,868) | (4,594) |
| Accounts payable and accrued liabilities | 660,590 | 7,046 |
| | 379,590 | 119,795 |
| | 2,816,641 | 626,867 |
| **Financing Activities** | | |
| Increase in bank debt | 1,500,000 | - |
| Issuance of share capital | 32,000 | 1,140,000 |
| Issuance costs | (6,419) | (7,300) |
| | 1,525,581 | 1,132,700 |
| **Investing Activities** | | |
| Capital expenditures | (4,880,787) | (5,101,729) |
| Net change in non-cash working capital for investing activities | (962,738) | 257,840 |
| | (5,843,525) | (4,843,889) |
| Decrease in cash | (1,501,303) | (3,084,322) |
| Cash and short term deposits, beginning of year | 1,428,423 | 4,512,745 |
| (Bank indebtedness) cash and short term deposits, end of year | $ (72,880) | $ 1,428,423 |
| Basic cash flow per Class A shares | $ 0.46 | $ 0.12 |
| Basic cash flow per Class A and Class B shares | $ 0.22 | $ 0.04 |
| Fully diluted cash flow per Class A and Class B shares | $ 0.22 | $ 0.04 |
| Interest paid | $ 34,552 | $ - |

See accompanying notes

# NOTES TO FINANCIAL STATEMENTS

**For the year ended December 31,1999**

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Company have been prepared in accordance with accounting principles generally accepted in Canada. The more significant of these accounting policies are the following:

### A] Petroleum and natural gas properties and equipment

The Company follows the full cost method of accounting in accordance with the guideline issued by the Canadian Institute of Chartered Accountants whereby all costs associated with the exploration for and development of oil and natural gas reserves are capitalized into a single Canadian cost centre and charged against earnings as set out below. Such costs include land acquisition, geological and geophysical, carrying charges of non-producing properties and costs of drilling both productive and non-productive wells and related overhead charges.

Gains or losses are not recognized upon disposition of oil and natural gas properties unless crediting the proceeds against accumulated costs would result in a change in the rate of depletion of 20% or more. Depletion is provided on costs accumulated in producing cost centres using the unit of production method. For purposes of the depletion calculation, gross proved oil and natural gas reserves, as determined by outside consultants, are converted to a common unit of measure on the basis of their approximate energy content.

The Company periodically reviews the costs associated with unproved properties and preproduction stage cost centres to determine whether they are likely to be recovered. When costs are not likely to be recovered, an impairment allowance is made or the value of these unproved properties is moved to the depletion pool.

The net carrying costs of the Company's oil and natural gas properties in producing cost centres is limited to an estimated recoverable amount. This amount is the aggregate of future net revenues from proved reserves and the costs of undeveloped properties, net of impairment allowances, less future general and administrative costs, financing costs, future site restoration costs and income taxes. Future net revenues have been calculated using prices in effect at the Company's year end without escalation or discounting.

### B] Joint venture accounting

Substantially all of the Company's petroleum and natural gas exploration and production activities are conducted jointly with others and, accordingly, the accounts reflect only the Company's proportionate interest in such activities.

### C] Capital assets

Capital assets are recorded at cost. Amortization is provided at the following rates and methods:

| | |
|---|---|
| Furniture and fixtures | 20% declining balance |
| Computer equipment | 20% declining balance |
| Office equipment | 20% declining balance |

### D] Future removal and site restoration costs

Estimated future removal and site restoration costs are provided for over the life of the proven reserves on a unit-of-production basis. Costs are estimated by management in consultation with engineers based on current regulations, costs, technology and industry standards. The annual charge is included in depletion and amortization expense and actual future removal and site restoration expenditures are charged to the accumulated provision account as incurred.

E] **Flow-through shares**

The deductions for income tax purposes of resource expenditures related to exploratory and development activities funded by flow-through share arrangements are renounced to investors in accordance with income tax legislation. Petroleum and natural gas properties and equipment and share capital are reduced by the estimated income taxes related to the renounced income tax deductions when the expenditures are incurred.

F] **Per share data**

Basic per share data per Class A shares is based upon the weighted average number of Class A shares outstanding during the period (1999 - 5,320,665; 1998 - 4,182,400). Basic per share data per Class A and Class B shares is based upon the weighted average number of Class A shares and the weighted average number of Class B shares outstanding during the period, converted at the December 31, 1999 trading price of $1.29 (1998 - $1) Class A shares (1999 - 10,846,052; 1998 - 11,310,150). Fully diluted per share data is based upon the weighted average number of Class A and Class B shares outstanding during the period after giving effect to the exercise of the share options and broker warrants (1999 - 11,178,260; 1998 - 11,811,430).

G] **Deferred income taxes**

The Company follows the deferred method of recording for income taxes. The Company will adopt the liability method for accounting for income taxes in the first quarter of year 2000.

H] Certain of the prior year's figures have been changed to conform with the current year presentation.

## 2. CAPITAL ASSETS

| | | 1999 | | 1998 |
|---|---|---|---|---|
| | Cost | Accumulated Depletion and Amortization | Net Book Value | Net Book Value |
| Petroleum and natural gas properties and equipment | **$ 10,092,038** | **$ 1,103,464** | $ 8,988,574 | $ 5,924,313 |
| Furniture and fixtures | **13,254** | **3,581** | 9,673 | 2,687 |
| Computer equipment | **13,722** | **5,800** | 7,922 | 7,821 |
| Office equipment | **505** | **247** | 258 | 323 |
| | **$ 10,119,519** | **$ 1,113,092** | $ 9,006,427 | $ 5,935,144 |

During 1999, the Company incurred $4,869,302 (1998 - $5,098,012) of capital expenditures related to petroleum and natural gas properties and equipment. This total has been adjusted by the tax effect of flow-through expenditures renounced to Class B shareholders in the amount of $577,176 (1998 - $1,473,128) and $505,020 to Class A shareholders.

During 1999, the Company capitalized $360,353 (1998 - $219,270) in overhead related costs to petroleum and natural gas properties and equipment.

Costs associated with unproven properties excluded from costs subject to depletion for 1999 totalled $320,807 (1998 - $119,698).

3. BANK DEBT

The bank debt consists of a line of credit with the National Bank of Canada for $3,100,000 at prime plus 1/2% per year. As of December 31, 1999 $1,500,000 (1998 - Nil) was outstanding. Interest paid during the year was $34,552. The terms of debt are such that no principal repayments are required if certain reserve levels are maintained. Consequently, all of the bank debt has been classified as long-term.

4. SHARE CAPITAL

A] **Authorized**

Unlimited number of Class A voting shares
Unlimited number of Class B subordinated voting shares

The Class B shares are convertible into Class A shares at a date to be selected by the issuer, between June 30, 2000 and June 30, 2002 and at the option of the Class B shareholder between July 1, 2002 and August 31, 2002. Any Class B shares outstanding on August 31, 2002 shall be automatically converted into Class A shares. The fraction of a Class A share obtained upon conversion of each Class B share will be equal to $10.00 divided by the greater of $1.00 and the current market price of a Class A share.

B] **Issued**

| Class A shares | Number of Shares | | Amount |
|---|---|---|---|
| Balance Class A shares, December 31, 1997 | 4,182,400 | $ | 761,268 |
| Obligation to issue Class A shares (Note 4c) | 1,140,000 | $ | 1,132,700 |
| Balance Class A shares, December 31, 1998 | 5,322,400 | $ | 1,893,968 |
| Issued for cash | 53,333 | $ | 32,000 |
| Share issue costs | - | $ | (6,418) |
| Tax effect of flow through | - | $ | (505,020) |
| Balance Class A shares, December 31, 1999 | 5,375,733 | $ | 1,414,530 |
| | | | |
| Class B shares | | | |
| Balance Class B shares, December 31, 1997 | 712,752 | $ | 5,395,013 |
| Tax effect of flow through | - | $ | (1,473,128) |
| Deferred income taxes | - | $ | 101,865 |
| Balance Class B shares, December 31, 1998 | 712,752 | $ | 4,023,750 |
| Tax effect of flow through | - | $ | (577,176) |
| Deferred income taxes | - | $ | 205,473 |
| Balance Class B shares, December 31, 1999 | 712,752 | $ | 3,652,047 |
| | | | |
| Total share capital, December 31, 1998 | - | $ | 5,917,718 |
| Total share capital, December 31, 1999 | - | $ | 5,066,577 |

During 1999, the Company incurred qualifying expenditures totalling $2,442,880 (1998 - $3,325,345).

In 1999, the Company incurred $1,302,880 of qualifying expenditures associated with the flow-through shares issued in the June 24, 1997 prospectus and $1,140,000 associated with the December 1998 private placement outlined in Note 4c. As a result of incurring these expenditures and renouncing them to the flow through share subscribers, Class A share capital and Class B share capital has been reduced by the tax effect of flow-through renunciation in the amount of $505,020 and $577,176 respectively and petroleum and natural gas properties have been reduced by $1,082,196.

### C] Obligation to issue share capital

Pursuant to a private placement in December 1998, the Company received $1,140,000 for subscriptions of 1,140,000 Class A flow through shares. In January 1999, the Company issued 1,140,000 Class A flow through shares for no additional consideration.

For financial statement presentation purposes, commissions of $7,300 have been netted against the gross proceeds of the private placement.

### D] Share options

The Company has granted officers, directors and consultants the following share options:

| Number of Options | Options Vested | Exercise Price Per Option | Expiry Date |
|---|---|---|---|
| 195,000 | 130,000 | $ 0.60 | April 15, 2002 |
| 99,667 | 48,667 | 0.60 | August 7, 2002 |
| 45,000 | - | $ 0.70 | February 19, 2004 |
| 53,333 | - | $ 1.50 | September 28, 2004 |

### E] Share purchase warrants

The Company had issued 383,200 share purchase warrants. Each warrant originally entitled the holder to purchase one Class A share for $1.25 until September 18, 1998. The expiry date was extended to December 18, 1998, however these warrants expired without being exercised. In addition, the Company has issued 153,280 broker warrants. Each broker warrant enables the Agent to purchase one Class A share for $1.00 until October 22, 1999 and these warrants expired without being exercised.

## 5. INCOME TAXES

The income tax expense in the Statement of Operations varies from the amount that would be computed by applying the expected income tax rate of 44.3% to earnings. The principal reasons for the difference between such "expected" income tax expense and the amount actually recorded are as follows:

| | **1999** | 1998 |
|---|---|---|
| Computed "expected" income tax expense | **$ 748,253** | $ 52,054 |
| Non-deductible crown charges | **75,101** | 6,743 |
| Non-deductible depletion | **161,767** | 87,441 |
| Resource allowance | **(256,583)** | (47,316) |
| Other | **(30,179)** | 2,943 |
| | **$ 698,359** | $ 101,865 |

The Company has approximately $177,000 of non-capital loss carry forwards which expire in 2004 and tax pools in respect of capital assets of approximately $3,238,000. In addition, the Company has available for deduction against taxable income share issue costs of approximately $296,000.

## 6. CONTINGENCY

The National Bank of Canada has provided letters of guarantee totalling $551,000 on behalf of the Company to third parties to cover completion costs, drilling costs and potential site restoration costs. The letters of guarantee expire between July 6, 2000 and November 1, 2000.

Subsequent to year end, letters of guarantee totalling $490,750 were cancelled.

## 7. COMMITMENT

The Company is committed to lease payments for occupancy costs and office equipment for the next four years as follows:

| | |
|---|---|
| 2000 | $ 54,577 |
| 2001 | 66,023 |
| 2002 | 49,141 |
| 2003 | 2,070 |

## 8. UNCERTAINTY DUE TO THE YEAR 2000 ISSUE

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. Although the change in date has occurred, it is not possible to conclude that all aspects of the Year 2000 Issue that may affect the entity, including those related to customers, suppliers, or other third parties, have been fully resolved.

## 9. FINANCIAL INSTRUMENTS

The Company's financial instruments that are included in the balance sheet are comprised of cash, accounts receivable, all current liabilities and bank debt.

**Fair values of financial assets and liabilities**
The fair values of financial instruments that are included in the balance sheet approximate their carrying amount due to the short-term maturity of those instruments.

**Credit risk**
A substantial portion of the Company's accounts receivable are with customers in the oil and gas industry and are subject to normal industry credit risks.

**Interest rate risk**
At December 31, 1999, the Company was exposed to interest rate fluctuations as interest on the Company's bank debt varies with changes in prime rate. A one percent variation in the interest rate would result in a $15,000 variance in the interest expense.

# CORPORATE INFORMATION



## DIRECTORS

**Steve Fitzmaurice***
Chairman of the Board
Calgary, Alberta

**Erik DeWiel**
Calgary, Alberta

**Randy Deobald**
Calgary, Alberta

**John Wright**
Calgary, Alberta

**Thomas Buchanan***
Calgary, Alberta

**Mike Shaikh***
Calgary, Alberta

**members of the audit committee*

## OFFICERS

**Steve Fitzmaurice, P.Eng.**
President, Chief Executive Officer

**Erik DeWiel, P.Land**
Vice President, Land and
Business Development

**Randy Deobald, P.Geol.**
Vice President, Exploration

**Greg Turnbull, L.L.B.**
Secretary

## OFFICE

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## AUDITORS

**PricewaterhouseCoopers LLP**
Calgary, Alberta

## BANKERS

**National Bank of Canada**
Calgary, Alberta

## ENGINEERING CONSULTANTS

**Outtrim Szabo Associates Ltd.**
Calgary, Alberta

## REGISTRAR AND TRANSFER AGENT

**Montreal Trust Company of Canada**
Calgary, Alberta

## SOLICITORS

**Gowling, Strathy & Henderson**
Calgary, Alberta

## STOCK EXCHANGE LISTING

**The Canadian Venture Exchange**
Trading Symbols:
**Class A Shares:** HWK.A
**Class B Shares:** HWK.B

## ABBREVIATIONS

| | |
|---|---|
| NGLs | natural gas liquids |
| bbls | barrels |
| mcf | thousand cubic feet |
| boe | barrels of oil equivalent |
| mbbls | thousand barrels |
| mmcf | million cubic feet |
| mboe | thousand barrel of oil equivalent (1bbl = 10mcf) |
| DCF | discount factor |
| $M | $ thousands |
| P/E | price to earnings ratio |
| WTI | West Texas Intermediate |
| mcfd | thousand cubic feet per day |
| bopd | barrels of oil per day |
| WI% | working interest percent |
| mmbtu | million British thermal units |
| NAV | net asset value |

# AN EYE ON PERFORMANCE

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